Sobeys Inc. 1999 Annual Report

a new scale of opportunity

Sobeys Inc. With 1,392 stores of which more than 900 are supermarkets in ten provinces, thousands of wholesale customers and the country's largest and only coast-to-coast foodservice operation, Sobeys is a brand-new giant in the Canadian food industry.

But we weren't born yesterday. Since J.W. Sobey opened his first butcher shop in Stellarton, Nova Scotia more than 90 years ago, the name Sobeys has stood for the best combination of service, selection and value in Atlantic Canada. With the December 1998 acquisition of The Oshawa Group Limited, a national food distributor with decades of experience in the business and a strong presence in the rest of Canada, Sobeys Inc. becomes the second largest food distributor in Canada with go forward proforma annual sales of $11 billion. This, our first annual report, explains how Sobeys plans to take advantage of its national scale to create immediate and long term value for its customers and shareholders.

Sobeys

Synergies made possible by the combination of Sobeys Inc. and The Oshawa Group Limited are expected to result in annual cost savings of $70 million. Half that amount will be realized by April 2000.

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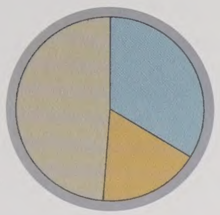
Sobeys

RETAIL SQUARE FOOTAGE

by Geographic Region

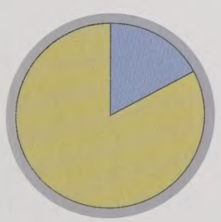
(14.1 million square feet)



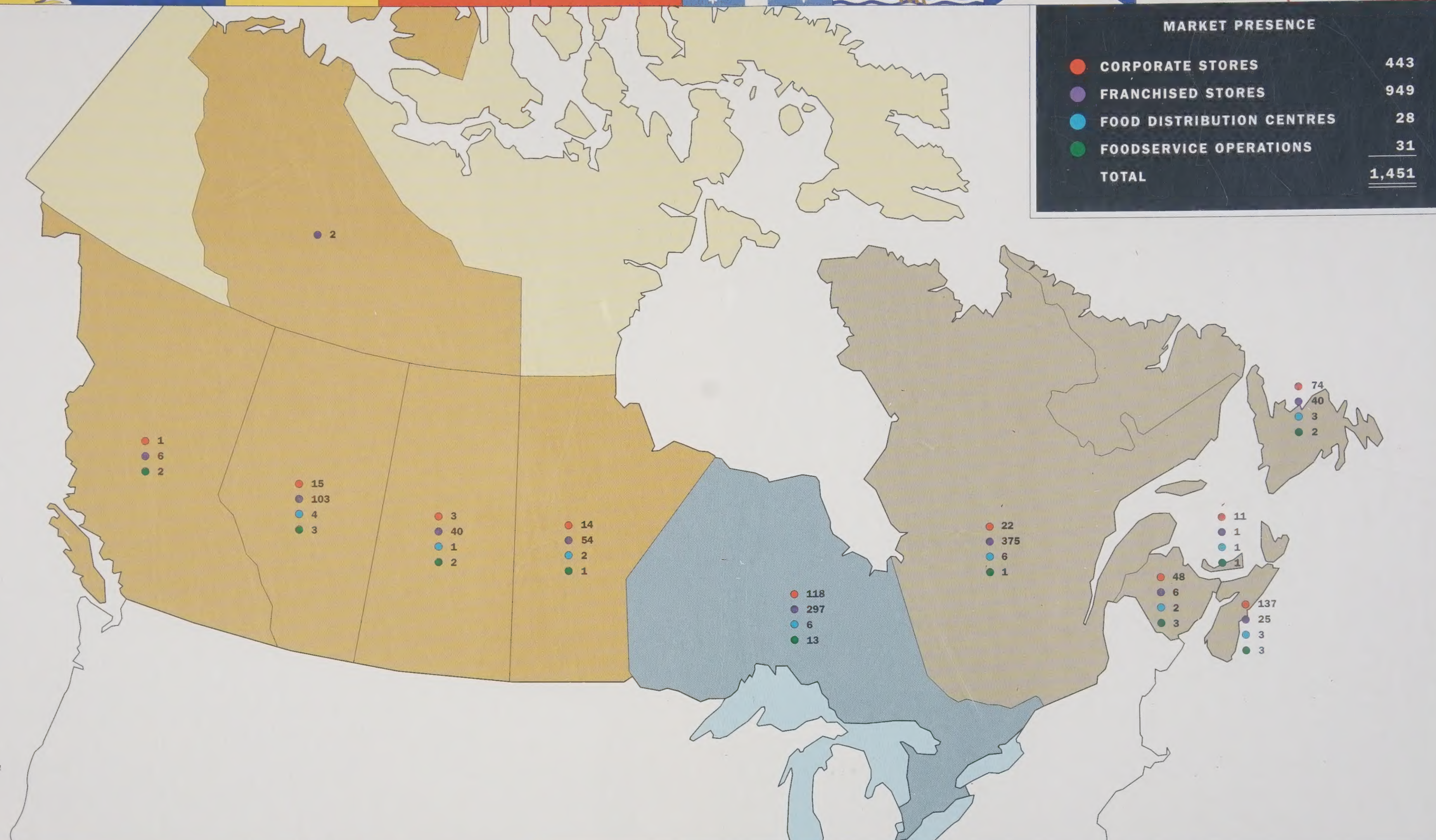
17.4% *Western Canada*
33.6% *Central Canada*
49.0% *Eastern Canada*

REVENUE

($6.23 billion)



83.0% *Food Distribution*
17.0% *Foodservice*



MARKET PRESENCE

CORPORATE STORES	443
FRANCHISED STORES	949
FOOD DISTRIBUTION CENTRES	28
FOODSERVICE OPERATIONS	31
TOTAL	1,451

NORTHERN AND WESTERN CANADA

Northwest Territories	
Food Town	2
Total	2

British Columbia	
IGA	6
Food Town	1
Total	7

Alberta	
IGA	102
Food Town	16
Total	118

Saskatchewan	
IGA	18
Food Town	23
Thrifty Foods	2
Total	43

Manitoba	
IGA	39
Food Town	27
Price Chopper	2
Total	68

CENTRAL CANADA

Ontario	
IGA	159
Sobeys	15
Knechtel	81
Foodland	49
Price Chopper	39
Price Check	25
Food Town	40
Other	7
Total	415

EASTERN CANADA

Quebec	
IGA	244
Sobeys	20
Boni Choix	123
Other	10
Total	397

New Brunswick	
Sobeys	23
Foodland	5
Needs & Green Gables	13
Lofood	5
Lawtons	8
Total	54

Nova Scotia	
Sobeys	36
Foodland	23
Needs & Green Gables	61
Lofood	5
Lawtons	37
Total	162

Prince Edward Island	
Sobeys	4
Needs & Green Gables	5
Lofood	2
Lawtons	1
Total	12

Newfoundland	
Sobeys	16
Foodland	38
Needs & Green Gables	40
Lawtons	20
Total	114

- Established Sobeys as a separate, publicly-traded company on December 9, 1998 with projected fiscal 2000 revenues of $11 billion.
- Purchased The Oshawa Group for $1.5 billion, adding 109 corporate and 838 franchised stores in western and central Canada to our Food Distribution network and acquiring Canada's largest and only national Foodservice operation.
- Identified $70 million in annual cost savings to be achieved through the effective integration of our new operation.
- Established 11 business planning transition teams to maximize potential savings, effectively guide the integration process and ensure the promotion of best practices throughout the Company.

Operating and Financial Highlights

($ in millions, except per share amounts)	1999	1998
Operations		
Revenue	6,231.8	3,155.1
Operating income	111.7	60.1
Earnings before restructuring and integration charge	39.1	37.3
Restructuring and integration charge	(47.1)	–
Net earnings	(8.1)	37.3
Operating cash flow before restructuring charge	122.1	80.6
Operating cash flow	36.9	80.6
Financial Position		
Total assets	2,878.8	922.9
Shareholders' equity	750.0	193.2
Per Share Information		
Earnings before restructuring and integration charge	1.07	1.65
Net earnings	(0.22)	1.65
Operating cash flow before restructuring charge	3.34	3.56
Operating cash flow	1.01	3.56
Book value	13.49	8:53
Share Price		
High	20.45	
Low	14.50	
Close	18.75	

Letter to Shareholders

A new scale of opportunity

On behalf of the board of directors, senior management and more than 32,000 employees from coast to coast, welcome to the inaugural annual report for the new Sobeys Inc.

Although this company came into being just a few short months ago, we are anything but a newcomer to the Canadian food distribution business. Sobeys Inc. is built on the rich heritage of two of the largest food distribution companies in Canada – the former Sobeys food distribution operations of Empire Company Limited and The Oshawa Group Limited. Together, they are being forged into a national food distribution and foodservice company, with a major market presence across the country and budgeted annual sales of $11 billion.

To explain why we are so excited about what the future holds – and just what we mean by the report's theme, a new scale of opportunity – it is important to first share with you the thinking behind the Company's creation.

The idea of Sobeys Inc. goes back to a strategic planning session that took place more than two and a half years ago. At the time, we were waging battle with a national competitor that was attempting to gain share in our home market of Atlantic Canada. A severe price war raged for 18 months and it was hard on our margins. When the dust settled, we had grown our share of the market from 42% to 45%. We were pleased with the performance of our employees and the loyalty of our customers, but our achievement had also confirmed a simple fact of life. As a regional player – no matter how dominant – we realized we would require significantly greater scale to maintain our leadership in the future.

At the same time, we recognized that the entry of new competitors into our market – both national supermarket chains and warehouse outlets – had led to an increase in retail square footage that was outpacing population growth. This development had already caused the elimination of some competitors and we could see that in our relatively mature market, further consolidation was inevitable. In today's business, consolidation and rationalization remains one of the best ways for successful companies to drive costs out of their operations while satisfying their customers rising expectations for service, selection and value.

So, recognizing the future direction of the industry, only two courses of action made sense to us. We could build our network as we have been doing on a limited scale in Ontario and Quebec, or significantly

(left to right): David F. Sobey, Chairman of the Board; Douglas B. Stewart, Vice-Chairman and Chief Executive Officer; John R. Sobey, President and Chief Operating Officer

expand the size and scope of our operations through a major acquisition. We chose the second route, because it gave us the immediate critical mass, as well as the diversification of revenue and earnings that we needed to maintain our leadership in a rapidly consolidating market.

But why The Oshawa Group? There were several compelling reasons. First, it was focused on food distribution and foodservice – the same lines of business in which we had decades of experience. At the same time, the combination would result in highly complementary geographic diversification, with minimal overlap between the two companies. Perhaps most important, Oshawa had long been recognized as a company with excellent retail locations and a good presence in rural and city markets. While results had been mixed in the past few years, recent efforts to improve the Company's profitability were already starting to bear fruit.

The important question now, of course, is how we intend to harness Sobeys' new scale to create enhanced value for our customers and shareholders. We see the opportunity to unleash significant benefits from the integration of Oshawa, in both the short and long term.

During the next two years, our strategy is to maximize the substantial synergies available through the careful integration of both companies. These include savings through the combined procurement of goods and services, reduced overhead, rationalization of the distribution network and the adoption of best practices throughout the organization. In total, we expect to achieve $35 million in annual savings by the end of fiscal 2000 and an additional $35 million in annual savings by the end of the following year. This is a conservative estimate based on achieving 75% of potential cost savings identified.

We recognize that some acquisitions do not fully achieve their original objectives. It is the skill with which companies are integrated that holds the key to success. That's why we engaged the services of a leading acquisition consultant early on in the process and quickly formed a number of transition teams to develop an integration strategy and timetable. Working together, we identified a core team of experienced leaders – from both sides of the business – to define key challenges and establish a critical path and timetable for meeting our goals. At this point, we are right on schedule in realizing our objectives. You can read more about our progress on pages 9 to 15 of this report.

Looking beyond the short term benefits of integration, we are also committed to strengthening Sobeys' position as a national leader in each of our businesses. During each of the next three years, Sobeys has budgeted significant capital spending to modernize and expand the size of our store network. The bulk of this spending will be concentrated in Ontario and Quebec to revitalize the "IGA" franchise network, to implement a state-of-the-art distribution system to service our retail network, and to further modernize the SERCA Foodservice operations.

With allowance for investment from Empire's real estate division, third party landlords and the combined investment of franchise owners, annual capital activity is projected to total $350 million to $450 million each year for the next three years.

Financial results

Sobeys' revenue increased 98% in fiscal 1999 to $6.23 billion while operating income was up 86% to $111.7 million. These results are not directly comparable to the previous year, of course, because they include 22 weeks of results from the former Oshawa operations as explained on page 17 in Management's Discussion and Analysis of the financial condition and performance of the Company.

Before an $85.1 pre-tax restructuring charge taken in the latter part of fiscal 1999 (see note 8, page 30, of the financial statements for details), net earnings increased 4.6% to $39.1 million or $1.07 per share. Net earnings are expected to increase significantly in fiscal 2000 primarily as the result of $35 million in pre-tax savings to be realized through the integration of our new operations.

As expected, the acquisition of The Oshawa Group required approximately $900 million in new debt. Combined with existing debt, this has resulted in a total debt level of $1.1 billion and a debt to capital ratio

Looking beyond the short-term benefits of integration, we are committed to strengthening Sobeys' position as a national leader in both its Food Distribution and Foodservice businesses.

of 59%. This is a higher level of leverage than we are used to and, as such, our objective is to reduce our debt load in as prudent a manner as possible through projected growth in cash flow as well as tighter management of working capital. With ample allowance for planned capital spending, our debt to capital ratio is expected to shrink from 59% to about 45% by the end of fiscal 2002.

Our people

To our delight, we have found a very strong management team in place at the former Oshawa Group operations. In fact, it has put us in the enviable position of being able to assemble a first-rate leadership team from some of the best people in the old Oshawa and Sobeys businesses. From The Oshawa Group, we have had the privilege of welcoming to our ranks such experienced practitioners as Pierre Croteau, Wayne Wagner and Bruce West, who are managing Sobeys franchise business in Quebec, western Canada and Ontario, respectively, and Gary Seaman, who is managing our national SERCA Foodservice operation. Thanks to their efforts, and the dedication of the people who report to them, we have already made progress in consolidating the Food Distribution and Foodservice operations into focused, national divisions.

These capable individuals join a team of industry respected Sobeys executives that includes Karl Sobey, who runs our Sobeys banner corporate stores across the country, and Darrell Rushton, President of our Atlantic Franchise Division. Together with John Lynn, our Executive Vice President of Human Resources and Corporate Affairs, Allan Rowe, Executive Vice President and Chief Financial Officer, and the rest of our executive management team, these individuals give us reason to be optimistic and confident about reaching our financial and operating targets on schedule.

We would also like to extend our welcome to our new franchise owners and our appreciation to the more than 32,000 employees who's efforts help ensure the success of the new company. Notwithstanding the substantial synergies that will result from integrating our operations across the country, it is the everyday commitment to excellence at the store level, that is the key to success in our business. In the course of meeting many store-owners and their employees during the past six months, we have been impressed with their dedication, as well as the spirit of optimism that has accompanied the recent change in ownership. Working together, we are confident that Sobeys is up to the challenges on the road ahead. On behalf of our customers, employees and shareholders, we fully intend to make the most of the new scale of opportunity before us.

Sincerely,

David F. Sobey,
Chairman of the Board

Douglas B. Stewart,
Vice-Chairman and
Chief Executive Officer

John R. Sobey,
President and
Chief Operating Officer


IGA
GARDEN
MARKET

Sobeys

SERCA

Price Chopper
Chop Your Grocery Bill
Bananas
39
Potatoes
95¢
1 69
4 49

IGA
IGA BEST PRICE Everyday

Sobeys' acquisition of The Oshawa Group Limited in December 1998 created a new national player in food distribution and foodservice, with projected sales of $11 billion, a significant market presence in every region of the country, and a position of unprecedented strength in a rapidly consolidating industry. One thing that hasn't changed, however, is the Company's time-tested approach to creating value for its customers and shareholders. This section of the report describes the basic elements of our strategy for profitable growth in the years ahead.

a new scale of opportunity

Investing in the future

While the $70 million in annualized savings to be generated through the effective integration of our new operations will drive a large part of the Company's earnings growth in the next two years, Sobeys' greatest opportunities are longer term in nature. For the first time, we are truly a national player, with a significant degree of geographic diversification. We possess a complete spectrum of complementary retail banners, extensive corporate and franchise operations spanning 10 provinces and the country's only national foodservice operation. Taking advantage of the unprecedented scale and reach of these businesses will be the key to sustained earnings growth.

In the retail Food Distribution business, 114 supermarkets operating under our corporate "Sobeys" banner meet the need for today's most demanding shoppers with a modern, full-service format. Up to 60,000 sq. ft. in size, these superstores feature farm-fresh produce, full-line bakeries, extensive home-style meal selections and a variety of innovative in-store retail services such as pharmacies, dry-cleaning and banking. They have been the key to success in our home market of Atlantic Canada and form the backbone of our growing corporate store operations in Quebec and Ontario.

With the addition of 568 stores under the "IGA" banner, strategically positioned from Quebec to British Columbia, Sobeys is also a major player in the neighborhood store segment of the market. Designed primarily for suburban and mid-size communities, "IGA" is a full-service supermarket in the 15,000 to 40,000 square foot range with emphasis on fresh departments and highly personalized service.

"Price Chopper" is our mid-size discount store in Ontario, ranging in size from 20,000 to 30,000 sq. ft. with all basic departments, but offering a limited assortment and fewer services. This banner is designed to serve price-driven consumers located in medium to large size urban areas. The discount segment of the market in Canada has grown rapidly in the past five years and the Company has kept pace with 41 stores currently under the Price Chopper banner and 14 new stores planned for fiscal 2000.

For smaller communities and inner-city markets across the country, our 422 franchised "Foodland", "Knechtel", "Food Town" and "Boni Choix" banners offer consumers a convenient, full-service supermarket on a smaller scale.

In combination with the thousands of company-owned, franchised and associated grocery and convenience stores supplied by our distribution network, these well-known retail banners give us the flexibility to meet the distinctive needs of different customer groups within a given community and thereby maximize our total share of the market.

Going forward, our priority will be to invest in the infrastructure and systems that will support the development of these banners. We are proceeding with the implementation of a multi-million dollar upgrade to our Ontario grocery distribution network. By February 2000, two state-of-the art, multi-temperature warehouses will be opened, a 495,000 sq. ft. Milton facility and a 438,000 sq. ft. Whitby facility. These ultra modern facilities, to be operated by third party distribution specialists, will lower distribution costs while providing single store order fulfillment and allowing the closure of three less efficient warehouses.

Subsequent to fiscal 2000 year-end, the Foodservice Group also plans to rationalize and streamline its Ontario food distribution structure by moving from 13 conventional warehouses to five efficient distribution facilities.

Information technology will also play a key role in Sobeys' success as an integrated, national player. Following two years of development, we began migration to SAP's advanced Enterprise Resource Planning (R3) software in January 1998. R3 is a multi-faceted software application that fully integrates key areas such as accounting, purchasing, inventory management, logistics, quality control and human resources. Integrating these processes is an important first step toward standardizing business practices, rationalizing our operations and ultimately, improving our efficiency and cost effectiveness. At present, we are on schedule to convert all of Sobeys' original retail and wholesale operations to the R3 enterprise-wide system by October 1999 and all of the former Oshawa operations by the end of fiscal 2001.

In addition to the SAP modules, we have installed EXE, a world class distribution software system, in 15 distribution centers with a coast-to-coast roll out scheduled to be completed by December 2000.

Unleashing the benefits of integration

In the food distribution industry, success depends on finding new ways to lower costs while delivering higher standards of service, quality and value to consumers. It's a recipe that has served Sobeys well particularly during the past 10 years, a period in which we maintained the leading share of the retail grocery market in Atlantic Canada while consistently lowering our operating costs. The acquisition of the Oshawa Group provides the opportunity to achieve similar results on an unprecedented scale, with $70 million in annual cost savings targeted by the end of fiscal 2001.

We are taking a studied approach to make the most of this challenge, realizing that the main reason many mergers fail to live up to expectations is not overestimating the benefits available but underestimating the effort required to ensure a smooth and efficient transition.

From the outset, we hired experienced post-merger consultants to help us plan and execute the integration process, taking care to select the best leaders from Sobeys and the former Oshawa operations. Eleven business planning transition teams were established with responsibility for identifying opportunities, setting

targets and minimizing costs in key areas such as national buying, category management, distribution, private label, corporate overhead and information systems.

According to our relatively conservative projections, these synergies will yield $35 million in annual savings by the end of fiscal 2000 and an additional $35 million in savings the following year. To date, we are right on target in meeting our objectives.

1. Better purchasing

Accounting for a material portion of planned integration savings are volume purchasing discounts associated with our sudden growth from a $3 billion to an $11 billion company. In addition, the Oshawa acquisition made us the key member in the IGA buying group, which is equivalent in size to any competitor in the country. Such benefits will extend to our controlled or private label program, which now represents a significant portion of total sales. The consolidation of our private label programs under the "Our Compliments"

Eleven business planning transition teams were established with responsibility for identifying opportunities, setting targets and minimizing costs in key areas such as national buying, category management, distribution, private label, corporate overhead and information systems.

line of premium products and the "Smart Choice" line of value-priced products is expected to lower the cost of goods from our suppliers while extending the range and enhancing the quality of our private label offering.

2. Cost reduction

More than half of planned integration savings in the next two years will come from streamlining our operations and eliminating duplication in areas such as human resources, administration, merchandising, advertising and marketing.

In the longer term, the rationalization of our distribution network and the implementation of enterprise wide information systems hold even greater promise for gains in efficiency.

3. Better management of working capital

At Sobeys, an unwavering focus on the balance sheet has long been one of the fundamental precepts of running our business. For example, three years ago we implemented a cash flow return on investment (CFROI) model to assess the performance of our operating management. Effective use of working capital is a big part of the model and as such, we continue to foster the implementation of effective working capital management policies throughout our operations.

4. Adoption of best practices

We are also excited by the benefits to be derived from the adoption of best practices throughout the company. The Oshawa and Sobeys operations both enjoyed regional loyalties based on the strength of many unique approaches to serving our customers. We have now begun to share this significant intellectual capital throughout the new organization. For example, Sobeys has long been an acknowledged leader in the application of technology in the grocery industry, from our pioneering efforts in the development of efficient consumer response to the installation of automated labour scheduling software in our corporate store network. Oshawa, in turn, has been an industry leader in the development of new retailing concepts such as private label development and its popular "Meals to Go" home meal replacement program.

Delivering more value to our customers

The integration of our operations also offers many opportunities to deliver more value to our customers, starting with the consolidation of our private label program. Although our private label brand name has now changed, the standard of quality will remain steadfast, and we look forward to enhancing our private label offering. To date, we have made significant progress in merging Sobeys "Our Best" and "Signal" lines into Oshawa's "Our Compliments" and "Smart Choice" brands, which enjoy national recognition and are offered in more than 1,400 stores across the country.

At the same time, we are taking the opportunity to pick the best from each line to create one of the most extensive private label programs in Canada. Our goal is to offer both premium products and value-based products that continue to offer our customers a distinct price advantage with a level of quality comparable to or better than national brands.

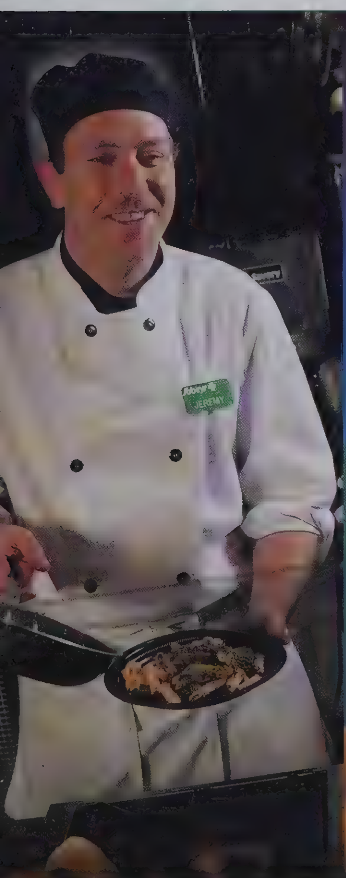
Such a program offers Sobeys many tangible benefits as well. For instance, the mere existence of a private label program provides enhanced negotiating power with national brand suppliers. In addition, because we control all branding and promotion, sales of private label brands are more profitable than national

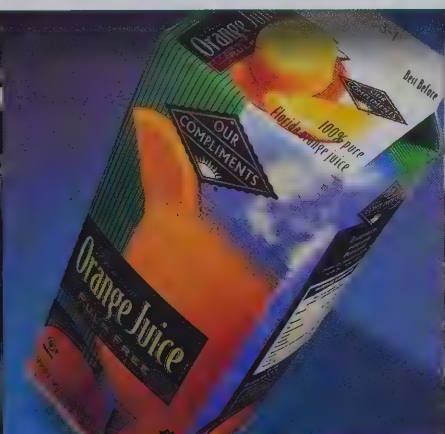
brands. They also help retain customer loyalty since they are only available in our networks. For these reasons the private label program continues to be a focal point in driving improved sales and profit margins.

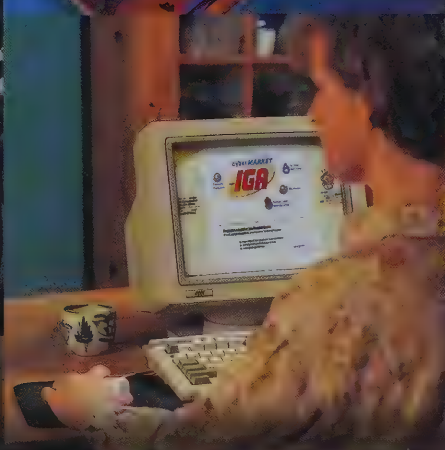
At the same time, we are taking care to pick the most successful retail formats from our regional Oshawa and Sobeys banners. Our objective is to profitably meet or exceed as many of our customer's needs as possible every time they walk into our stores. For example, IGA's "Meals to Go" and Sobeys "Meals Made Easy" programs offer today's time-pressed shoppers a delicious variety of ready-to-serve, home-cooked meals. In formats such as Sobeys' "Courtyard", which has been rolled out to selected stores, shoppers can take the time to sample an appetizing range of premium quality foods including fresh baked pizza, rotisserie chicken, hot and cold pasta entrees, a wide selection of fruit and vegetable salads, gourmet coffees and a variety of tempting desserts.

Picking the best also means making use of new distribution channels. First launched in 1997, the "IGA Cybermarket" is Canada's first home grocery shopping site on the Internet (www.iga.net), with the trial participation of some 130 stores in the province of Quebec. It provides a new level of convenience by

From the integration and expansion of our private label program to the creation of innovative retail formats, we continue to find new ways to meet the changing needs of our customers.







allowing customers to place their orders from home or work, with the local "IGA" store serving as the point of pick-up or delivery.

Another way to make sure our customers keep coming back is "Club Sobeys". In the past year, this advanced customer loyalty program has grown to include about one million members. For our customers, "Club Sobeys" offers the advantages of sweepstakes promotions, electronic couponing, frequent shopper bonus points and many other benefits. In return, the program allows us to develop a comprehensive database that helps us better design future promotions and continue to find better ways to meet our customer's changing needs.

During the past year, the program continued to be rolled out in Ontario and Quebec and by the end of calendar 1999, all Sobeys stores will be part of the program. We also see tremendous potential in the broader rollout of a "Club Sobeys" style loyalty program by making these benefits available to our IGA network.

Meanwhile, the Company's Foodservice operation is finding new ways to deliver enhanced value to its customers while increasing Sobeys' "share of stomach". The largest and only national foodservice company in Canada, SERCA is focused on serving the needs of national and regional food chains, independent restaurants, institutional customers such as hospitals and long term care facilities, and corporate cafeterias. Within these growing segments of the market, SERCA's ability to offer consistent quality, systems and service on a national scale has become an increasingly important advantage. The Company continues to build on its leadership position through many customer-focused initiatives such as one of the industry's most extensive private label programs and an automated ordering technology that now extends to the Internet.

Working smarter every day

In today's increasingly competitive retail environment, the status quo is never an option. With the continuous launch of new products and the introduction of retailing space at a rate that exceeds population growth, consumers have wider choice than ever before. Success depends on continuous innovation – constantly finding new ways to lower cost and deliver better value to our customers.

At Sobeys, harnessing new technology has long been a key part of our approach. We were pioneers in efficient consumer response (ECR) – an industry wide effort that has linked producers, distributors and retailers in an effort to drive costs out of the supply chain. Today, we are extending our leadership with the implementation of Vision 2020, a comprehensive enterprise wide management system using SAP/EXE which will provide a common integrated platform for our Food Distribution and Foodservice businesses. At present, all former Sobeys operations are expected to be converted to the new system by October, 1999. Although the former Oshawa Group distribution systems are now considered Year 2000 compliant, we also plan to convert these operations to our SAP/EXE system by the end of fiscal 2001.

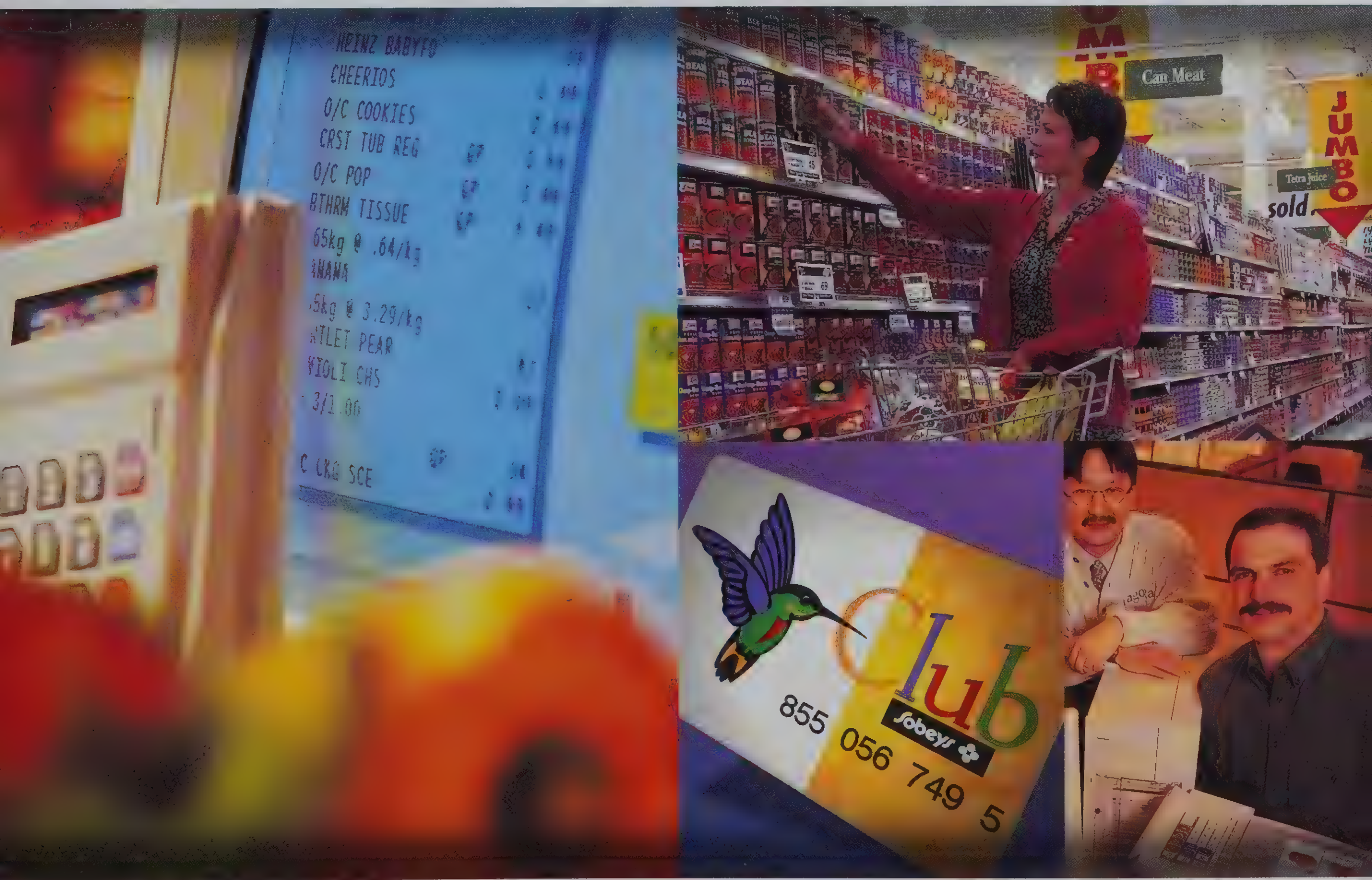
The installation of SAP/EXE will make possible the utilization of a host of related technologies. Our new point-of-scale scanning system, which has been installed in all Sobeys stores, is a good example. The new system will give us SKU-level data by transaction, by customer. That means we will be able to examine our business right down to the real-time status of every item, on every store shelf, in every market.

Such technology also is key to our efforts to better understand and satisfy the needs of our customers through the "Club Sobeys" loyalty program. Thanks to the quality of information generated by the new

system, we are able to track the unique needs and preferences of each customer. Such capabilities are aiding our efforts to develop a true one-to-one relationship with our customers, where mass advertising can be replaced with tailored promotional offers ("micro-marketing") based on their own shopping pattern.

Finally, the point-of-sale system and related technologies will provide valuable pricing and other information to our category managers – who approach each type of product we sell – from paper towels to dry pasta – as an individual business. We continue to manage each section of the store shelf – working with vendors, adjusting prices, applying incentives, and choosing the right mix of national and private label brands – in order to maximize the sales and profitability of each category. The implementation of the new point-of-sale technology, and the enhanced data made available through our Club Sobeys program, will better position our category managers to understand and respond to the needs of our customers.

Our advanced point-of-sale scanning technology is aiding efforts to develop true one-to-one relationships with our customers, where mass advertising can be replaced with tailored promotional offers based on individual shopping patterns.



financial review

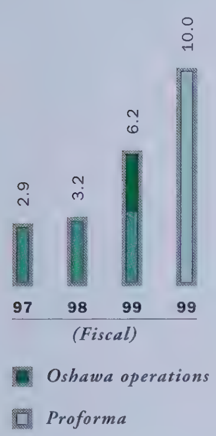
Management's Discussion and Analysis

Sobeys Inc. This section of the report provides management's discussion and analysis of the current financial condition of Sobeys Inc. ("Sobeys" or "the Company") and its financial performance for the year ended May 1, 1999. As part of this discussion, we assess the outlook of each business segment, the current financial condition of the Company, and the impact of risks. This discussion should be read in conjunction with the consolidated financial statements, including the notes that accompany them found on pages 23 to 33.

The fiscal 1999 financial performance of Sobeys (including results of operations, sales, operating income and net earnings) includes the results of 22 weeks of The Oshawa Group Limited ("Oshawa") operations and are therefore not directly comparable to the prior year.

Sobeys

SALES
($ billions)



On a proforma basis, the combined Sobeys/Oshawa business would generate $10.0 billion in annual sales for fiscal 1999.

Business strategy

Sobeys is the second largest food distributor in Canada in terms of sales, number of supermarkets and geographic presence, and the country's only national foodservice distributor.

The Company's goal is to exceed our customers expectations by operating the best Food Distribution and Foodservice businesses in Canada – to be market driven, focused on superior execution, and supported by effective operations.

Prior to its acquisition of Oshawa in December 1998, Sobeys pursued growth outside its core Atlantic Canadian market, principally in Quebec and Ontario, for many years through small acquisitions and internal expansion. By the end of the Company's fiscal 1998, in fact, more than 30% of the Company's food distribution revenues were derived outside Atlantic Canada.

With the establishment of Sobeys Canada Inc. (subsequently renamed Sobeys Inc.) on October 27, 1998, and the offers by Sobeys to purchase all of the issued shares of Oshawa in November 1998, the stage was set for the Company's growth and diversification on a much larger scale.

In December 1998, Sobeys acquired the voting and non-voting shares of Oshawa for approximately $1.5 billion (as explained in note 2 of the financial statements). At that time, Sobeys became a public company with 62% ownership by Empire Company Limited. The Oshawa acquisition will provide the geographic scope, range of store formats, product diversity and complementary competencies to enable Sobeys to serve its customers better and compete more effectively with larger players in central and western Canada. As a national player, the Company should benefit in the years ahead from revenue diversification and increased financial strength and added financial flexibility. This acquisition is also expected to enhance the Company's position relative to the ongoing consolidation taking place in the North American food distribution industry.

The acquisition of Oshawa was accounted for using the purchase method, as explained in note 2 of the financial statements. This has resulted in the inclusion of 22 weeks of Oshawa's results from the date of the acquisition.

Results of operations

During fiscal 1999, Sobeys Inc. opened or replaced 8 new Sobeys banner stores, and 7 new IGA banner stores. An additional 10 Sobeys banner stores and 15 IGA banner stores were renovated or expanded. As a result, at the end of fiscal 1999, the Company operated 1,392 stores comprised of 443 corporate stores and 949 franchised stores, 28 distribution centres and 31 Foodservice operations. The acquisition of Oshawa, which added 9.5 million retail square feet, combined with the new stores opened during the year and the renovation of existing stores, resulted in the Company's total retail selling area increasing to 14.1 million square feet, from 4.3 million square feet in fiscal 1998, a 228% increase in net retail selling area.

Sales

Sales for the combined Food Distribution and Foodservice businesses totaled $6.23 billion in fiscal 1999, a 98% increase over last year. The majority of this increase is due to the inclusion of 22 weeks of Oshawa's operations (which increased sales by 88% or $2.8 billion). For this 22 week period, Oshawa's sales increased 5.4% over the same period last year. On a comparable basis, excluding 22 weeks of Oshawa results, total sales increased by 9.1% for fiscal 1999. On a proforma basis, the inclusion of Oshawa's operations for a full year would generate $10.0 billion in annual sales for the Company in fiscal 1999.

($ millions)	F99	F98
Sales		
Food Distribution	$ 5,173.5	$ 2,747.3
Foodservice	1,058.3	407.8
	$ 6,231.8	$ 3,155.1
Operating Income		
Food Distribution	$ 95.6	$ 46.2
Foodservice	16.1	13.9
	$ 111.7	$ 60.1

OPERATING INCOME
Fiscal 1999
($111.7 million)

85.6% *Food Distribution*
14.4% *Foodservice*

Operating income

Before a restructuring charge of $85.1 million, operating income (EBIT or earnings before interest and taxes) increased 86%, reaching $111.7 million in fiscal 1999. This increase was primarily the result of increased sales volume from the Oshawa acquisition. The Company recorded an operating income margin (EBIT/Sales) of 1.79% and a trading margin (EBITDA/Sales – or earnings before interest, taxes, depreciation and amortization divided by sales) of 3.10% in fiscal 1999, compared to an operating income margin of 1.91% and a trading margin of 3.35% earned in the prior year. Included in this year's results is a 22 week contribution from Oshawa, which produced a 1.73% operating income margin and a 2.76% trading margin over the period.

Depreciation and amortization expense

Depreciation and amortization expense increased by 80% to reach $81.8 million in fiscal 1999. Expressed as a percentage of sales, depreciation and amortization expense dropped to 1.31% in fiscal 1999, compared with 1.44% in fiscal 1998. The reasons for the dollar increase in depreciation and amortization expense are: (i) the inclusion of Oshawa's results for the 22 weeks ended May 1, 1999, which added $26.3 million to depreciation expense; (ii) goodwill increased by $736 million as a result of the Oshawa acquisition, increasing amortization by $8.0 million from the prior year; and (iii) Sobey's capital expenditure program totaling $265.8 million, which added $2.1 million to depreciation expense. The previous factors are expected to add $41.4 million to depreciation and amortization expense in fiscal 2000.

Financing costs

Financing costs amounted to $46.3 million in fiscal 1999, a $35.5 million increase from the $10.8 million recorded last year. Interest on long term debt increased $30.4 million over last year. Interest on short term debt, net of interest income, increased by $5.1 million from the prior year. The increase in interest expense from fiscal 1998 is primarily as a result of the increased debt required to finance the acquisition of Oshawa. Sobeys is committed to a debt reduction program that will lower the cost of borrowing as further explained in the debt section of this analysis.

Net earnings

Net loss for the 1999 fiscal year amounted to $8.1 million ($0.22 loss per share), a $45.4 million decrease in earnings from the $37.3 million recorded in fiscal 1998. Excluding the after tax restructuring charge of $47.1 million, net earnings increased 4.6% to $39.1 million or $1.07 per share. Net earnings are forecast to increase in fiscal 2000, primarily as a result of the $35 million pre-tax savings expected to be realized from the successful integration of the former Sobeys and Oshawa businesses.

Segmented results

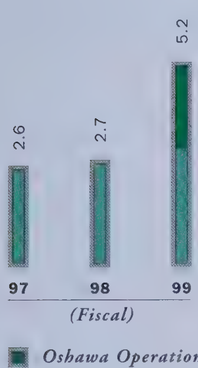
Sobeys operates principally in two business segments: (i) Food Distribution, consisting of 83% of Sobeys total fiscal 1999 sales and 86% of its total operating income, and (ii) Foodservice, consisting of 17% of total fiscal 1999 sales and 14% of its operating income. The Food Distribution segment consists of the distribution of food products throughout all provinces. The Foodservice segment also distributes foodservice products to customers in all provinces of Canada.

Food Distribution

Sales

Food Distribution sales grew by $2.43 billion or 88% to reach $5.17 billion in fiscal 1999. $2.18 billion of the increase resulted from the inclusion of Oshawa results for the 22 weeks since the acquisition while 8.8% growth in the former Sobeys operation added $250 million. Same-store sales for all banners increased by 2.9%. After adjusting for the effects of food price inflation of 1.3%, real same store sales for all banners increased by 1.6%. The Company's fiscal 1999 Food Distribution sales are not directly comparable to fiscal 1998, as a result of the inclusion of Oshawa sales for 22 weeks in fiscal 1999. For this 22 week period, Oshawa's Food Distribution sales increased 5.2% over the same period last year. On a comparable basis, after excluding the impact of the 22 weeks of Oshawa's results, total sales increased 5.7% from fiscal 1998.

SALES
FOOD DISTRIBUTION
($ billions)



The inclusion of 22 weeks of Oshawa results added $2.2 billion to Food Distribution sales in fiscal 1999.

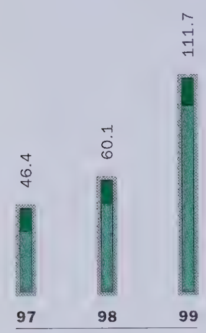
Same store sales	Before inflation	Adjusted for 1.3% food inflation
All banners	2.9%	1.6%
Sobeys store banner	3.9%	2.6%
IGA store banner	2.7%	1.4%

This growth was supported by $265.8 million in combined capital expenditures, including an increase in total retail store square footage of 268,000. The Oshawa acquisition also added 9.5 million retail square feet and $94.9 million in additional capital expenditures since the acquisition.

During fiscal 1999, as part of its sales growth initiatives, the Company continued to enhance its "Club Sobeys" loyalty program. This program rewards customers with additional discounts on selected featured items as well as Club points that can be redeemed for future grocery purchases. The Company intends to expand the "Club Sobeys" concept, eventually making this benefit available across the IGA network. Increased use of the "Club Sobeys" loyalty database to support targeted marketing efforts is considered important to the Company maintaining and enhancing its customer base.

The acquisition of Oshawa added 109 corporate stores and 838 franchised stores, significantly expanding the Company's base in Quebec and Ontario as well as creating a presence in western Canada. As of the end of fiscal 1999, the Company has a total of 1,392 stores, comprised of 443 corporate stores and 949 franchised stores. The Company's stores now operate under 12 corporate and franchised retail banners including "IGA," "Sobeys," "Foodland," "Price Chopper," "Boni Choix," "Knechtel," "Price Check Foods," "Lofood Stores," "Needs," "Green Gables," "Food Town," and "Lawtons Drugs." In total the Oshawa acquisition tripled the number of corporate and franchised stores. The acquired corporate stores average 26,100 square feet in size whereas the average size of the acquired franchised stores is 12,300 square feet.

OPERATING INCOME
($ millions)



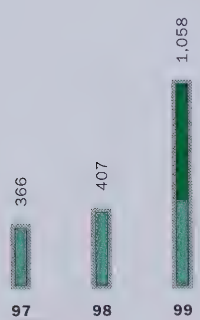
(Fiscal)

Food Distribution

Foodservice

After the inclusion of 22 weeks of Oshawa results in fiscal 1999, operating income grew by 86%.

SALES FOODSERVICE
($ millions)



(Fiscal)

Oshawa Operations

The inclusion of 22 weeks of Oshawa results added $606 million to Foodservice sales in fiscal 1999.

Banners	Corporate stores	Franchised stores	Totals
IGA	64	504	568
Sobeys	114	–	114
Foodland	4	111	115
Price Chopper	41	–	41
Knechtel	2	79	81
Price Check	25	–	25
Lawtons	60	6	66
Food Town	–	109	109
Lofood	11	1	12
Needs & Green Gables	118	1	119
Boni Choix	2	121	123
Other banners	2	17	19
Totals	443	949	1,392

The Company's retail capital expenditure program in fiscal 2000 includes plans to increase the total combined retail square footage by 8.5%, resulting in over 15 million retail square feet. By the end of fiscal 2000 the distribution of retail square footage by region is expected to be: Atlantic Canada 17.8%, Quebec 29.6%, Ontario 34.2%, and Western Canada 18.4%.

Operating income

In fiscal 1999, Food Distribution operating income (EBIT) was 1.85% of sales or $95.6 million compared with 1.68% or $46.2 million in fiscal 1998. The bulk of this percentage increase is attributable to a continued focus on reduction of operating expenses. In addition, operating income was positively affected by continued expansion of the Company's private label sales.

Foodservice

Sales

Foodservice sales for fiscal 1999 amounted to $1.06 billion, an increase of 159% over last year. Inclusion of the results of Oshawa for 22 weeks added $606 million or 93% of the $651 million increase. For this 22 week period, Oshawa Foodservice sales increased 6.2% over the same period last year. After excluding 22 weeks of the Oshawa operations, total sales increased by 11% for fiscal 1999 due to growth in each of the geographic areas served by the former Sobeys businesses.

Operating income

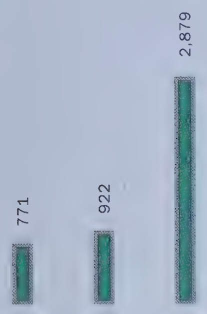
In fiscal 1999, Foodservice operating income (EBIT) was 1.52% of sales compared with 3.42% in fiscal 1998. The Company's fiscal 1999 operating income is not comparable to fiscal 1998 due to the inclusion of: (i) 22 weeks of Oshawa's operations for the current year and (ii) profit from internal supply arrangements in the prior year. The impact of the Oshawa acquisition accounted for 1.38 percentage points of this change whereas the former Sobeys business accounted for 0.52 percentage points of the difference. Traditional internal supply arrangements with the Food Distribution operations have been realigned and after reflecting the national scope of the Foodservice business, fiscal 2000 operating income is budgeted to reach 1.80% of sales.

Liquidity and capital resources

Cash provided by operating activities was $260.0 million in fiscal 1999, compared with $91.7 million last year. The increase in fiscal 1999 was primarily due to the Oshawa acquisition.

Cash flows used in investing activities increased to $1.53 billion in fiscal 1999, compared with $79.8 million in fiscal 1998. The increase in investing activities over the prior year was primarily due to the acquisition of Oshawa.

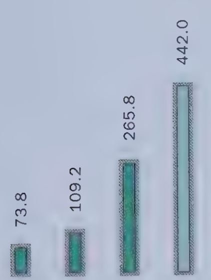
TOTAL ASSETS
($ millions)



(Fiscal)

Total assets tripled in fiscal 1999 primarily as a result of the Oshawa acquisition.

CAPITAL SPENDING
($ millions)



(Fiscal)

2000 Projection

With the inclusion of 52 weeks of Oshawa, capital spending is expected to increase to $442 million ($150 million in Sobeys direct capital expenditures and $292 million in franchisee and third party financing).

Other capital expenditures (net of disposals) increased by $115.1 million in fiscal 1999 to reach $196.6 million. The Company equipped a total of 15 new stores and renovated 10 existing stores while 11 new stores and 15 renovated stores were added as a result of the Oshawa acquisition. In total, the Company opened 26 new and renovated 25 stores in fiscal 1999.

The Company plans to continue its growth plan, which focuses on a combination of new store openings and renovations, as well as growth through acquisitions as appropriate. The Company expects to open 53 new stores, replace 18 older stores and renovate approximately 237 stores in fiscal 2000. Capital project activity for fiscal 2000 is expected to total $442 million, supported by $292 million in franchise and third party lease financing and $150 million in Sobeys direct capital expenditures. Capital activity includes approximately $125 million on new and replacement store construction, $118 million on renovations and over $146 million on warehouse related expenditures. The balance of the capital budget is earmarked for information technology and minor store expenditures.

Cash flows provided by financing activities increased to $1.3 billion in fiscal 1999, compared to cash flow used for financing of $15.2 million in fiscal 1998. The increase in fiscal 1999 was primarily the result of the issue of $913.7 million in long term debt and $404.3 million in common shares to finance the Oshawa acquisition.

The Company plans to finance capital spending for fiscal 2000 through funds from operations, existing bank credit lines, franchisee third party leases, and operating leases. At year-end, the Company maintained bank credit facilities in excess of borrowings of $178 million.

Debt

The Oshawa acquisition and capital expenditure program necessitated substantial increases in debt levels over last year. Short term debt, comprised of bank loans and bankers' acceptances, increased $32.0 million to reach $122.5 million at year-end. Long term debt, comprised of $800 million in seven year non-revolving term debt and $173.9 million of other long term debt, as described in note 6 of the financial statements, increased $832.7 million over fiscal 1998.

Sixty percent of the bank credit long term debt is scheduled to be repaid over the next seven years. Realization of forecast earnings improvement coupled with this long term debt repayment schedule is expected to improve the financial condition of the Company. Existing credit facilities include an annual ratio test which grants a 37.5 basis point reduction in the interest rate charged on the debt for each five percentage point decline in the debt-to-capital ratio. Debt is prepayable at anytime without penalty. Planned debt repayments will positively impact net income through significantly reduced interest expense.

Risk and risk management

The most significant operating risk affecting the Company is the potential for reduced revenues and declining profit margins as a result of intense competition given the mature structure of the Canadian food distribution industry. To mitigate this risk, the Company's strategy is to be geographically diversified with a national presence, to be market-driven, to be focused on superior execution and to be supported by cost effective operations. The Company is committed to tailoring its offerings to meet changing customer needs as well as providing consumers with greater value and product diversity.

Sobeys has two significant national operations in the food industry, Food Distribution (corporate and franchise) and Foodservice which provides a measure of diversification and balance of earnings should competition in a particular region or sector intensify or the economies of a region or sector change.

The recent acquisition of Oshawa has presented Sobeys with many integration challenges and opportunities. Management believes that the planned integration savings from the combination of the two companies of $35 million in fiscal 2000 and an additional $35 million in fiscal 2001 will be realized.

In addition, Sobeys have adopted a number of key financial policies to manage financial risk. For example: in the ordinary course of managing its debt, the Company has entered into various interest rate and currency swaps, which are not reflected on the balance sheet. As explained in note 6 of the financial statements, the effect of these interest rate swaps is to fix the rate the Company pays on $800 million of debt.

Sobeys is self-insured for limited risks while maintaining comprehensive loss prevention and management programs to mitigate retained risks. The range of non-insured related risk exposure is not anticipated to be material to the overall operations of the Company.

The Company completes an ongoing comprehensive environmental compliance report and is not aware of any significant environmental liabilities.

As explained in note 2 to the financial statements, as a result of the Oshawa acquisition the Company's foodservice operations in Atlantic Canada and a small number of food stores in Quebec and Ontario are currently under review by the Competition Bureau. The Company anticipates no material loss of business will occur upon completion of this review.

Certain forward-looking statements are included in this annual report relating to capital expenditures, cost reduction, operating improvements and year 2000 compliance. Such statements are subject to inherent uncertainties and risks, including but not limited to: business and economic conditions generally in the Company's operating regions; pricing pressures and other competitive factors; results of the Company's ongoing efforts to reduce costs; the ability to integrate the newly acquired Oshawa operations; and the availability and terms of financing. Consequently, actual results and events may vary significantly from those included in or contemplated or implied by such statements.

Year 2000

The Company has been evaluating its information technology and other systems and equipment to identify and adjust date sensitive systems for year 2000 compliance. A year 2000 project team has been created and is lead by staff from the Company's information technology department as well as representatives from other areas of the Company. The year 2000 team has developed a four-phase plan to effectively resolve any year 2000 issues. These phases consist of assessment, remediation, testing and implementation.

The assessment, remediation and testing phases are complete with final implementation in all divisions scheduled by the end of calendar 1999. Sobeys has undertaken a complete system review as part of its strategy to address year 2000 issues.

The total cost of implementing the information technology plans, including year 2000 compliance, is not expected to have a material impact on the financial condition of the Company.

The Company cannot assure with absolute certainty that there will not be an adverse impact on operations if third parties do not appropriately address their year 2000 issues in a timely manner.

Although the Company does not believe the actual impact of any system failures related to the century change will be material, various contingency plans have been developed with critical suppliers to ensure the timely delivery of inventory and prepare for normal business activities following the century change. These plans include alternate means of communication with suppliers, manual operation of certain systems, as well as the implementation of contingency ordering procedures. Under the terms of these ordering procedures, critical suppliers will provide inventory to the Company based on historical ordering patterns. These suppliers will also substitute products and adjust inventory levels of substitute items based on the availability of certain products. The Company will continue to develop and finalize the implementation of its contingency plans with third parties throughout 1999.

The Company's response to year 2000 issues is believed adequate to mitigate all known material risks related to the century change. However, due to inherent uncertainties surrounding these issues, Sobeys is unable to rule out any material adverse year 2000-related impact on the operations, earnings and financial condition of the Company.

Outlook

As a result of the addition of Oshawa, management expects to achieve significant economies of scale. The Company believes that this acquisition will generate increased savings through synergies in purchasing, administration and technology, and by streamlining our capital expenditures. Important benefits are also expected from identifying and sharing best practices across the new Company. Sobeys' integration model was based on the achievement of $70 million in annual pretax synergies within a two year period, $35 million of which will be generated during our first full year of operation commencing May 2, 1999.

The Canadian grocery distribution industry operates under a mature market structure. Competition is intense, however there are currently no major price wars, as large players concentrate on integration issues and food price inflation is low. Sobeys' focus in this environment is to: (i) emphasize the effective integration of its operations and acquisitions, (ii) reduce product and operational costs (iii) prudently rationalize its' banners, (iv) concentrate on improving distribution network efficiencies, and (v) enhance the Company's banner positioning.

The opportunities associated with the planned successful integration of the Sobeys and Oshawa businesses are meaningful. Accordingly we look for continued growth in earnings in future years.

Management's Responsibility for Financial Reporting

Preparation of the consolidated financial statements accompanying this annual report and the presentation of all other information in the report is the responsibility of management. The financial statements have been prepared in accordance with appropriate and generally accepted accounting principles and reflect management's best estimates and judgements. All other financial information in the report is consistent with that contained in the financial statements.

The Board of Directors, through its Audit Committee, oversees management in carrying out its responsibilities for financial reporting and systems of internal control. The Audit Committee, which is chaired by and includes a majority of non-management directors, meets regularly with financial management and external auditors to satisfy itself as to the reliability and integrity of financial information and the safeguarding of assets. The Audit Committee reports its findings to the Board of Directors for consideration in approving the annual financial statements to be issued to shareholders. The external auditors have full and free access to the Audit Committee.

Douglas B. Stewart
Vice-Chairman and
Chief Executive Officer
June 22, 1999

Allan D. Rowe
Executive Vice President and
Chief Financial Officer
June 22, 1999

Auditors' Report

To the Shareholders of Sobeys Inc.

We have audited the consolidated balance sheets of Sobeys Inc. as at May 1, 1999, May 2, 1998 and May 3, 1997, and the consolidated statements of earnings, retained earnings, and changes in financial position for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at May 1, 1999, May 2, 1998 and May 3, 1997, and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Grant Thornton
Chartered Accountants

New Glasgow, Nova Scotia
June 14, 1999

(in thousands) May 1	1999	1998	1997
ASSETS			
Current			
Cash	$ 71,133	$ 27,176	$ 30,413
Marketable securities, at cost (quoted market value $5,445; 1998 $316,095; 1997 $215,635)	4,546	315,205	215,205
Receivables	394,323	77,289	65,562
Income taxes recoverable	9,623	–	–
Inventories	462,122	190,289	183,314
Prepaid expenses	31,284	8,446	8,454
Due from parent company	–	9,950	12,462
	973,031	628,355	515,410
Investments and advances (Note 3)	144,633	9,853	9,758
Property and equipment (Note 4)	868,942	273,069	235,220
Goodwill (less accumulated amortization of $18,850)	734,335	4,676	5,308
Deferred income taxes	87,413	6,960	4,831
Deferred costs	70,463	–	–
	$ 2,878,817	$ 922,913	$ 770,527
LIABILITIES			
Current			
Bank loans (Note 5)	$ 7,485	$ –	$ –
Bankers' acceptances (Note 5)	115,000	40,500	37,500
Commercial paper	–	50,000	48,000
Accounts payable and accrued charges	1,013,017	292,531	265,040
Income taxes payable	–	5,467	3,145
Long term debt due within one year	74,031	7,953	8,088
Due to parent company	–	200,000	100,000
	1,209,533	596,451	461,773
Long term debt (Note 6)	899,874	133,277	140,356
Minority interest	–	–	171
Deferred revenue (Note 1)	19,421	–	–
	2,128,828	729,728	602,300
SHAREHOLDERS' EQUITY			
Capital stock (Note 7)	647,207	66,801	66,801
Deferred foreign exchange translation gain (loss)	(230)	1,368	756
Retained earnings	103,012	125,016	100,670
	749,989	193,185	168,227
	$ 2,878,817	$ 922,913	$ 770,527

See accompanying notes to the consolidated financial statements.

On Behalf of the Board

Director

Director

Consolidated Statement of Retained Earnings

(in thousands) Year Ended May 1	1999	1998	1997
Balance, beginning of year	$ 125,016	$ 100,670	$ 86,278
Net earnings (loss)	(8,074)	37,339	26,870
	116,942	138,009	113,148
Dividends paid	13,930	12,993	12,478
Balance, end of year	$ 103,012	$ 125,016	$ 100,670

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Earnings

(in thousands) Year Ended May 1	1999	1998	1997
Sales	$ 6,231,838	$ 3,155,084	$ 2,947,574
Cost of sales, selling and administrative expenses	6,038,344	3,049,530	2,858,182
Depreciation and amortization	81,817	45,408	42,963
Operating income	111,677	60,146	46,429
Interest expense			
Long term debt	46,104	15,749	17,433
Short term debt	197	(4,918)	(5,402)
	46,301	10,831	12,031
	65,376	49,315	34,398
Restructuring and integration charge (Note 8)	(85,143)	–	–
Operating earnings (loss) before the following items	(19,767)	49,315	34,398
Investment income	1,074	4,409	2,031
Minority interest (expense)	–	(10)	(7)
	(18,693)	53,714	36,422
Income taxes (recovery) (Note 9)			
Restructuring and integration charge	(38,017)	–	–
Other operations	27,398	16,375	9,552
	(10,619)	16,375	9,552
Net earnings (loss)	$ (8,074)	$ 37,339	$ 26,870
Earnings per share (Note 10)	$ (0.22)	$ 1.65	$ 1.19

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Changes in Financial Position

(in thousands) Year Ended May 1	1999	1998	1997
Cash provided by (used for) operations			
Net earnings (loss)	$ (8,074)	$ 37,339	$ 26,870
Items not affecting cash (Note 11)	83,010	43,271	41,835
Restructuring and integration charge net of income taxes of $38,017	47,126	–	–
Operating cash flow before restructuring and integration charge	122,062	80,610	68,705
Restructuring and integration charge (Note 8)	(85,143)	–	–
Operating cash flow	36,919	80,610	68,705
Net change in other current items	223,031	11,119	14,041
Total cash provided by operations	259,950	91,729	82,746
Cash provided by (used for) financing			
Bank loans	7,485	–	(16,403)
Bankers' acceptances	74,500	3,000	(1,975)
Commercial paper	(50,000)	2,000	8,000
Issue of long term debt	913,656	597	–
Repayment of long term debt	(214,032)	(7,811)	(11,967)
Issue of capital stock	580,406	–	–
Receipt of deferred revenue	13,200	–	–
Payment of dividends	(13,930)	(12,993)	(12,478)
Total cash provided by (used for) financing	1,311,285	(15,207)	(34,823)
Total cash available	1,571,235	76,522	47,923
Cash used for (provided by) investments			
Property, equipment and other assets	265,839	109,197	73,838
Proceeds on disposal of fixed assets	(69,213)	(27,672)	(22,640)
Long term investments and advances	4,755	(7)	412
Increase in deferred costs	27,736	–	–
Marketable securities	(38,222)	–	–
Business acquisitions, net of cash acquired	1,461,945	1,176	15,279
Decrease (increase) in deferred foreign currency translation gains	(612)	(594)	(388)
Parent company preference shares and note receivable (Note 12)	(124,950)	(2,512)	(30,116)
Buy-out of minority interest	–	171	–
Total cash used	1,527,278	79,759	36,385
Increase (decrease) in cash	43,957	(3,237)	11,538
Cash, beginning of year	27,176	30,413	18,875
Cash, end of year	$ 71,133	$ 27,176	$ 30,413
Operating cash flow before restructuring and integration charge per share (Note 10)	$ 3.34	$ 3.56	$ 3.03

See accompanying notes to the consolidated financial statements.

May 1, 1999
All notes in thousands except share capital

1. Accounting policies

Principles of consolidation

These consolidated financial statements include the accounts of the Company and all subsidiary companies. Marketable securities are accounted for on the cost basis.

Depreciation

Depreciation is recorded on a straight line basis over the estimated useful lives of the assets as follows:

Equipment and vehicles	3 – 10 years
Buildings	15 – 40 years
Leasehold improvements	7 – 10 years

Inventories

Warehouse inventories are valued at the lower of cost and net realizable value with cost being determined on a first-in, first-out basis. Retail inventories are valued at the lower of cost and net realizable value less normal profit margins as determined by the retail method of inventory valuation.

Leases

Leases meeting certain criteria are accounted for as capital leases. The imputed interest is charged against income and the capitalized value is depreciated on a straight line basis over its estimated useful life. Obligations under capital leases are reduced by rental payments net of imputed interest. All other leases are accounted for as operating leases with rental payments being expensed as incurred.

Goodwill

Goodwill represents the cost of investments in subsidiary companies in excess of fair value of the underlying assets at date of acquisition. Goodwill is amortized on a straight line basis over its estimated life of 40 years.

The Company evaluates the carrying value of goodwill by considering whether the amortization of the goodwill balance over its remaining life can be recovered through undiscounted future operating cash flows of the acquired operation(s).

Interest capitalization

Interest related to the period of construction is capitalized as part of the cost of the related building. The amount of interest capitalized to construction in progress in the current year was $391; 1998 $327; 1997 $392.

Deferred revenue

Deferred revenue consists of a long term purchase agreement and rental revenue arising from the sale of subsidiaries. Deferred revenue is being taken into income over the term of the related agreement and leases.

Foreign currency

Assets and liabilities of self-sustaining foreign investments are translated at exchange rates prevailing at the balance sheet date. The revenues and expenses of the foreign operations are translated at average exchange rates prevailing during the year. The gains and losses on translation are deferred and included as a separate component of shareholders' equity titled "deferred foreign exchange translation gain/loss."

Development and store opening expenses

Development and opening expenses of new stores and store conversions are written off during the first year of operation.

Information systems development costs

Costs directly attributable to the development of core information system projects are capitalized and amortized over their estimated useful life of seven years. As at May 1, 1999 these costs were included in fixed assets in the amount of $47.3 million. This project began in 1998 and no amortization has been recorded to date. The new system will be fully operational in May 2000 at which time amortization will occur.

Accounting estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future.

2. Business acquisition

Sobeys Inc. ("Sobeys"), formerly Sobeys Canada Inc., was incorporated on October 27, 1998 as a wholly owned subsidiary of Empro Holdings Limited ("Empro"), an indirect wholly owned subsidiary of Empire Company Limited. On November 2, 1998 Sobeys acquired all the issued and outstanding shares of Sobeys Capital Inc. ("Sobeys Capital") from Empro for consideration of 22,646,500 common shares. This acquisition has been accounted for as a continuity of interests and is treated in a manner similar to a pooling of interest. At the date of the combination, Sobeys had nominal assets and net book value, while Sobeys Capital had total assets of $980 million, total liabilities of $773 million and a net book value of $207 million.

On November 2, 1998 Sobeys acquired 972,700 Class "A" non-voting shares of The Oshawa Group Limited ("Oshawa") from Empro for $24 million, representing the carrying value of the shares held by Empro.

During the period from December 1, 1998 to January 25, 1999, Sobeys acquired all the remaining issued and outstanding Class "A" shares and all the issued and outstanding common shares of Oshawa, for combined consideration of cash of $1.1 billion and 21,252,502 common shares valued at $380 million. This acquisition has been accounted for by the purchase method under which the results from operations of Oshawa, since the date of acquisition, have been included in Sobeys financial statements. Details of the acquisition are as follows:

Fair value of identifiable assets acquired	$ 1,494,543
Less identifiable liabilities assumed	713,044
Fair value of identifiable net assets acquired	781,499
Goodwill	736,208
Total purchase consideration	$ 1,517,707
Consideration representing:	
Cash	$ 1,113,413
Common shares	404,294
	$ 1,517,707

Certain aspects of the Company's acquisition of Oshawa are currently under review by the Competition Bureau. Specific foodservice operations in the Maritimes and a small number of food stores in local Ontario and Quebec markets are being examined. The Company anticipates that no material loss of business will occur upon completion of the review. If necessary, any gain or loss arising from a possible Competition Bureau ruling, will be reflected as an adjustment to the purchase price allocation.

3. Investments and advances

	1999	1998	1997
Loans receivable	$ 92,479	$ 9,439	$ 9,220
Mortgages receivable	51,640	–	–
Other	514	414	538
	$ 144,633	$ 9,853	$ 9,758

Loans receivable

Loans receivable represent long term financing to certain retail associates. These loans are primarily secured by inventory, fixtures and equipment, bear interest at rates which fluctuate with prime and have repayment terms up to ten years. The carrying amount of the loans receivable approximates fair value based on the variable interest rates charged on the loans and the operating relationship of the associates with the Company.

Mortgages receivable

The majority of the mortgages receivable balance relates to the sale of 24 retail properties by The Oshawa Group in calendar 1997. These mortgages of $50,300 are for a term of 3 years and bear interest at 5.25%. Principal repayment is due on maturity.

The loans and mortgages receivable are net of a current portion of $14,010.

4. Property and equipment

	1999 Cost	1999 Accumulated Depreciation	1999 Net Book Value	1998 Cost	1998 Accumulated Depreciation	1998 Net Book Value	1997 Net Book Value
Land	$ 93,308	$ –	$ 93,308	$ 8,588	$ –	$ 8,588	$ 8,339
Land held for development	60,151	–	60,151	35,784	–	35,784	23,446
Construction in progress	21,340	–	21,340	13,475	–	13,475	9,399
Buildings	310,863	88,463	222,400	87,951	30,418	57,533	58,366
Information system development costs	47,290	–	47,290	10,270	–	10,270	–
Equipment	998,705	655,695	343,010	376,588	243,135	133,453	123,066
Leasehold improvements	171,300	94,164	77,136	30,311	17,148	13,163	12,028
Assets under capital leases	7,189	2,882	4,307	3,784	2,981	803	576
	$1,710,146	$ 841,204	$ 868,942	$ 566,751	$ 293,682	$ 273,069	$ 235,220

5. Bank loans and bankers' acceptances

Under the terms of a credit agreement entered into between the Company and a banking syndicate arranged by the Bank of Nova Scotia, a revolving term credit facility was established. This facility will expire on December 8, 1999, however various provisions of the agreement provide the Company with the ability to extend the facility for a minimum period of two years.

Interest is payable on this facility at rates which fluctuate with changes in the prime rate.

As security for this facility and the secured bank loans provided under the credit agreement, the Company has provided a fixed and floating charge over all assets, subject to permitted encumbrances, a general assignment of book debts and the assignment of proceeds of insurance policies.

6. Long term debt

	1999	1998	1997
First mortgage loans, average interest rate 10.0%, due 1999 – 2016	$ 33,931	$ 23,899	$ 25,430
Secured bank loans, average interest rate 8.2%, due Dec. 9, 2005	800,000	–	–
Debentures, average interest rate 10.9%, due 2003 – 2013	109,338	115,900	121,675
Notes payable and other debt at interest rates fluctuating with the prime rate	17,529	425	558
	960,798	140,224	147,663
Capital lease obligations, due 1999 – 2003, net of imputed interest	13,107	1,006	781
	973,905	141,230	148,444
Less amount due within one year	74,031	7,953	8,088
	$ 899,874	$ 133,277	$ 140,356

6. Long term debt (continued)

The Company has fixed the interest rate on $204.4 million of its long term debt at 8.4% for 3 years and has fixed the interest rate on $595.6 million of its long term debt at 8.2% for 7 years by utilizing interest exchange agreements.

Long term debt is secured by land and buildings, specific charges on certain assets and additional security as described in Note 5. Debt retirement payments and capital lease obligations in each of the next five fiscal years are:

	Long term debt	Capital leases
2000	$ 71,497	$ 2,534
2001	67,884	2,559
2002	98,250	2,271
2003	97,886	1,170
2004	105,799	1,023

Operating leases

The net aggregate, annual, minimum rent payable under operating leases is approximately $119,681 ($180,693 gross less of expected sub-lease income of $61,012).

7. Capital stock

	Number of shares
Authorized	
During the year the Company created the following authorized capital:	
Preferred shares, par value of $25 each, issuable in series as a class	500,000,000
Preferred shares, without par value, issuable in series as a class	500,000,000
Common shares, without par value	500,000,000
1998 and 1997	
Preferred shares par value of $10 each, non-cumulative, redeemable, issuable in series as a class	905,681
Common shares, without par value	1,000,000
Common shares, par value of $100 each	667,997

Issued and outstanding

	Number of shares			Capital stock (in thousands)		
	1999	1998	1997	1999	1998	1997
Common shares, without par value	55,596,617	–	–	$ 647,207	$ –	$ –
Common shares, without par value	–	207	207	–	1	1
Common shares, par value of $100 each	–	667,997	667,997	–	66,800	66,800
Total capital stock				$ 647,207	$ 66,801	$ 66,801

Comparative figures for 1998 and 1997 represent the authorized and issued and outstanding amounts for Sobeys Capital Inc.

During the year the Company issued the following common shares:

a) 22,646,500 to a subsidiary of Empire Company Limited (parent company) in exchange for common shares of Sobeys Capital Inc., of which $68,835,000 was allocated to share capital.

b) 21,252,502 as partial consideration for common shares of The Oshawa Group Limited of which $379,888,473 was allocated to share capital.

c) 1,959,004 to a subsidiary of Empire (parent company) for common shares of The Oshawa Group of which $24,405,626 was allocated to share capital.

d) 9,738,610 to a subsidiary of Empire (parent company) for cash consideration of $174,077,673.

8. Restructuring and integration charge

Subsequent to the acquisition of The Oshawa Group Limited on November 30, 1998, the Company commenced a comprehensive review of its strategic direction, facilities and staffing levels of all operations of the combined organizations. This integration initiative was undertaken to create

8. Restructuring and integration charge (continued)

operating efficiencies, cost savings and revenue enhancement opportunities. This project, which was substantially complete in April 1999, brought together the operating groups of both business units and generated a new business plan for the future. In connection with the integration initiative, the Company recorded a $85.1 million charge ($47.1 million after tax) in the fourth quarter for restructuring and integration. The amount remaining in liabilities as at May 1, 1999 is $69.2 million.

Foodservice Segment

$45.2 million of the restructuring and integration charge relates to the Foodservice segment and involves the rationalization of operations and modernization of the distribution supply network. These activities are scheduled to commence late in 1999 and continue until early 2001. The charge to exit these activities is comprised of severance and other obligations to employees, lease commitments for closed locations and other charges.

Food Distribution Segment

The remaining charge of $39.9 million relates to the Food Distribution segment. The rationalization of Ontario operations accounts for the majority of this charge. It includes severance and other obligations to employees and other charges resulting from the closure of 17 smaller marginal stores in Ontario, the franchising of 56 corporate owned stores and the streamlining of certain department operations in Ontario. Substantially all of these activities are scheduled to commence in early fiscal 2000 and be completed by year end. The remaining charge for the Food Distribution segment includes severance and other costs associated with the roll out of Sobeys' common information systems across acquired business units. Systems implementation is scheduled to commence in early 2000 and end in mid 2001.

9. Income taxes

The effective rate of corporate income taxes varies from statutory rates as a result of the receipt of intercorporate dividends, the amortization of goodwill being non-deductible for income tax purposes and the large corporation tax of $1,285 (1998 $383; 1997 $399).

10. Earnings and cash flow per share

Earnings and cash flow per share amounts are calculated on the weighted average number of shares outstanding (1999 – 36,518,471; 1998 and 1997 – 22,646,500 representing the shares exchanged in 1999 as described in Note 2).

	1999	1998	1997
Earnings before restructuring and integration charge	$ 39,052	$ 37,339	$ 26,870
Restructuring and integration charge net of income taxes of $38,017	(47,126)	–	–
Net earnings (loss)	$ (8,074)	$ 37,339	$ 26,870
Earnings per share is comprised of the following:			
Earnings before restructuring and integration charge	$ 1.07	$ 1.65	$ 1.19
Restructuring and integration charge net of income taxes	(1.29)	–	–
Net earnings (loss)	$ (0.22)	$ 1.65	$ 1.19

11. Items not affecting cash

	1999	1998	1997
Depreciation and amortization	$ 81,817	$ 45,408	$ 42,963
Deferred income taxes	(7,584)	(2,129)	(951)
Gain (loss) on disposal of assets	(2,191)	(8)	(177)
Writedown of fixed assets	10,300	–	–
Amortization of deferred items	668	–	–
	$ 83,010	$ 43,271	$ 41,835

12. Related party transactions

The Company leased certain real property from related parties during the year. The aggregate net payments under these leases amounted to approximately $45,535 (1998 $39,880; 1997 $39,795). The Company was charged expenses of $60 (1998 $80; 1997 $80) by related parties. The Company had sales to related parties of $671 (1998 $846; 1997 $8,411) and made purchases of $767 (1998 $716; 1997 $717) from related parties.

On November 30, 1998, prior to Sobeys acquisition of 100% of the capital stock of The Oshawa Group Limited, $315,000 of preferred shares of the parent company (Empire) were redeemed, $9,950 due from parent company was repaid and $200,000 due to parent company was repaid.

For 1997 and 1998, these intercompany investments (preferred shares and note receivable) have been shown as "other assets" in the "identifiable assets" section of Note 15.

Interest expense paid on the due to parent company was $6,627 in 1999 (1998 $6,946; 1997 $5,087).

Interest income received on the due from parent company was $501 in 1999 (1998 $1,027; 1997 $1,262).

13. Financial instruments

Foreign exchange contracts

The Company utilizes financial instruments which are not reflected on the balance sheet to reduce foreign exchange risks on its U.S. long term debt. At May 1, 1999, $194.9 million U.S. was covered by such instruments with $43.2 million U.S. maturing in 2002 and $151.7 million U.S. maturing in 2005.

The fair value of the foreign exchange agreements represents the amount the Company would pay or receive to terminate the agreements. At May 1, 1999, the estimated payment on termination is $11.0 million U.S. based on market conditions.

All the financial instrument contracts are with Canadian Schedule 1 Banks thereby controlling the Company's credit risk exposure.

Other financial instruments

The book value of cash, receivables, income taxes recoverable, bank loans, bankers' acceptances and accounts payable and accrued charges approximate fair values at May 1, 1999. The fair value of marketable securities is $5.45 million.

The total fair value of long term debt is estimated to be $999.4 million. The fair value of variable rate long term debt is assumed to approximate its carrying amount. The fair value of other long term debt has been estimated by discounting future cash flows at a rate currently offered for debt of similar maturities and credit quality.

14. Contingent liabilities

Uncertainty due to the year 2000 issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range form minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the year 2000 issue affecting the entity, including those related to the efforts of customers, suppliers or other third parties, will be resolved.

Guarantees and commitments

The Company has undertaken to provide cash to meet any obligations which Sobey Leased Properties Limited (a wholly owned subsidiary of Empire Company Limited) is unable or fails to meet until all of its debentures have been paid in full in accordance with their terms. Any deficiency payment made by the Company will be by purchase of fully-paid non-assessable 5% redeemable, non-voting preference shares of that company. The aggregated outstanding principal amounts of these debentures at May 1, 1999 is $48,770.

At May 1, 1999 the Company was contingently liable for letters of credit issued in the aggregate amount of $18,000.

15. Segmented information

	1999	1998	1997
Sales			
Food Distribution	$ 5,173,516	$ 2,747,308	$ 2,581,361
Foodservice	1,058,322	407,776	366,213
	6,231,838	3,155,084	2,947,574
Operating income			
Food Distribution	95,559	46,217	32,084
Foodservice	16,118	13,929	14,345
	111,677	60,146	46,429
Identifiable assets			
Food Distribution	1,766,838	513,906	465,210
Foodservice	377,644	79,381	72,547
Other (Note 12)		324,950	227,462
Goodwill	734,335	4,676	5,308
	2,878,817	922,913	770,527
Depreciation and amortization			
Food Distribution	73,299	42,206	39,368
Foodservice	8,518	3,202	3,595
	81,817	45,408	42,963
Capital expenditures			
Food Distribution	249,159	105,575	71,697
Foodservice	16,680	3,622	2,141
	$ 265,839	$ 109,197	$ 73,838

The Company operates principally in two business segments, Food Distribution and Foodservice. The Food Distribution segment consists of the distribution of food products throughout all provinces of Canada. The Foodservice segment also distributes foodservice products to customers throughout Canada.

16. Pension plan

The Company maintains a defined contribution plan and a number of defined benefit pension plans. Current actuarial estimates indicate the pension benefits under the defined benefit plan at May 1, 1999 are $165,624 and the pension fund assets, using the moving average market value are $169,926.

17. Subsequent events

Immediately following the year end, the two operating subsidiary companies amalgamated. Subsequently, the Company changed its name to Sobeys Inc.

18. Comparative figures

Comparative figures have been reclassified, where necessary, to reflect the current year's presentation.

Executive Directors

DAVID F. SOBEY (4)
Chairman, Sobeys Inc.

DONALD R. SOBEY (4)
Chairman, Empire Company Limited

JOHN R. SOBEY (4)
President and COO,
Sobeys Inc.

PAUL D. SOBEY (2)(6)
President and CEO,
Empire Company Limited

DOUGLAS B. STEWART (4)
Vice-Chairman and CEO,
Sobeys Inc.

Independent Directors

JOHN L. BRAGG (1)
Collingwood, Nova Scotia
President, Oxford Frozen Foods Limited

MARCEL CÔTÉ (4)
Montreal, Quebec
Senior Partner,
Secor Inc.

SIR GRAHAM DAY (5)
Hantsport, Nova Scotia
Counsel to Stewart
McKelvey Stirling Scales

ROBERT P. DEXTER (2)(6)
Halifax, Nova Scotia
Chairman and CEO,
Maritime Travel (Group) Limited

HUGH G. FARRINGTON (3)
Cape Elizabeth, Maine
President and CEO,
Hannaford Bros. Co.

RONALD V. JOYCE (4)
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J. WILLIAM RITCHIE (2)
Halifax, Nova Scotia
Chairman, Keltic Inc.

LAWRENCE N. STEVENSON (6)
Toronto, Ontario
President and CEO,
Chapters Inc.

ANNETTE VERSCHUREN (4)
Toronto, Ontario
President, Home Depot Canada

(1) Audit Committee Chairman
(2) Audit Committee Member
(3) Human Resources Committee Chairman
(4) Human Resources Committee Member
(5) Integration Committee Chairman
(6) Integration Committee Member

Officers

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Chairman

DOUGLAS B. STEWART
Vice-Chairman and CEO

JOHN R. SOBEY
President and COO

ALLAN D. ROWE
Executive Vice President and CFO

KARL R. SOBEY
President,
Corporate Retail Operations

DARRELL M. RUSHTON
President, Atlantic Division

PIERRE CROTEAU
President, Quebec Division

BRUCE WEST
President, Ontario Division

WAYNE A. WAGNER
President, Western Division

GARY H. SEAMAN
President, SERCA Foodservice Inc.

JOHN K. LYNN
Executive Vice President,
Human Resources and
Corporate Affairs

DARRELL R. EWERT
General Counsel and Secretary

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Investor Relations
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www.empireco.ca

Shareholders' Annual Meeting
September 8, 1999 at 10:00 a.m.
Aberdeen Cinemas
610 East River Road
New Glasgow, Nova Scotia

Stock Exchange Listings
The Toronto Stock Exchange
Montreal Exchange

Stock Symbols
Common Shares - SBY

Average Daily Trading Volume (TSE)
140,000

Common Dividend Record and Payment Dates for Fiscal 2000*

Record Date	Payment Date
July 15, 1999	July 30, 1999
Oct. 15, 1999	Oct. 29, 1999
Jan. 14, 2000	Jan. 31, 2000
Apr. 14, 2000	Apr. 28, 2000

* subject to approval by Board of Directors

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